



Douglas County Internal Audit

December 24, 2013

Douglas County Board of Commissioners
1819 Farnam Street, Suite LC2
Omaha, NE 68183

Attention: Mary Ann Borgeson, Mike Boyle, Clare Duda, Marc Kraft, PJ Morgan,
Chris Rodgers and Pam Tusa

Dear Commissioners and Officials:

I have completed an audit of the County's contract monitoring processes. The purpose of the audit was to assess the processes used by the County to monitor contract performance and verify the accuracy of the related vendors' billings. The audit revealed that the lack of a consistent process resulted in varying levels of effectiveness. Opportunities to improve controls were identified and appear below.

Background

The monitoring of contracts within the County is decentralized. Each department where contractual goods or services are received is responsible for monitoring contract compliance. Monitoring for compliance includes making sure that:

- Vendors provide goods and services according to contractual specifications.
- Performance bonds and insurance policies protecting the County are properly maintained.
- Appropriate reporting is provided.
- Vendor billings reflect the actual receipt of goods and services provided and the accurate extension of prices and quantities.

In 2011 the County purchased contract database software from Cobblestone Systems. A Contract Administrator is responsible for populating the database. The intent is for all County contracts to reside in the Cobblestone database. Appropriate data input enables the software to automatically alert assigned personnel to help ensure that contract renewal or other efforts are undertaken to secure an uninterrupted flow of goods and services. Cobblestone is also used by personnel in the Clerk/Comptroller office to help them in their audit of invoices.

Objective

The purpose of the audit was to determine if:

- There were effective county-wide contract monitoring policies and procedures in place.
- There was effective monitoring over specifically selected contracts.
- The contract database was being used effectively to aid departments with contract oversight.

Scope

The processes used as of November 2013 to populate the Cobblestone database and by each department to monitor the selected contracts were assessed. Six current contracts were judgmentally selected to test for effective monitoring by individual departments. The six contracts selected were:

- Midwest Independent Physicians – provides nursing, physicians, and physician assistants personnel to the Primary Healthcare Network Clinic
- Lifecare Family Medicine of Bellevue – provides consultations, histories and physicals for clients at the Community Mental Health Center
- Payless Office Products – provides office supplies
- Petroleum Traders – provides unleaded gasoline
- Aramark Correctional Services – provides all inmate meals at the Correctional Center
- Waste Management of Nebraska – operates the County Landfill

Additionally, twenty-five invoices from the first and second quarter of fiscal year 2014 were judgmentally selected to test for billing accuracy according to the contract terms of the six contracts identified above.

Methodology

The information documented by Internal Audit was obtained through interviews and observations of the policies and procedures in place as of the date identified in the scope. Contracts and related documents were obtained from the Cobblestone database, department personnel, and vendor submissions. Along with an assessment of the policies and procedures as provided, tests were performed to verify contract compliance and billing accuracy. The tests included but were not limited to the following steps below:

- The data input into the Cobblestone database was compared to the contracts to determine if it was entered accurately.
- Departmental procedures were assessed for adequacy and to determine if there was evidence of a consistent county-wide policy in place for monitoring contract compliance.
- Performance bonds, professional licenses, and insurance certificates were obtained to see that they were current and agreed to contract terms.
- Invoices and supporting documentation was obtained to determine if there was evidence to support the receipt of goods and services included in vendor billings.
- Billing rates agreed to contractual rates, and the invoices were properly extended.

The issues identified appear in the Findings section below:

Findings

Policies and Procedures

Criteria: Management should define and communicate the necessary policies and guidelines needed to effectively monitor contract compliance including vendor billings.

Condition: There were no county-wide policies or guidelines in place to help ensure that all departments had effective contract monitoring and billing verification processes in place. Various aspects of contractual terms and billings were not effectively monitored. Specific findings related to the contracts tested appear below:

- The monthly tonnage that Waste Management billed for was reconciled to landfill reports and Waste Management's records. The individual category tonnages and rates were not verified.
- The yearly public evaluation of Waste Management was not conducted.
- The County did not track the actual number of gallons delivered by Petroleum Traders to determine when the contractual quantity was met.
- The Petroleum Traders certificate of insurance obtained only listed workers compensation coverage and did not include the County as an additional insured. (The Petroleum Traders contract required that the city of Omaha be included as an additional insured but not the County.)
- The discount/gross margin for Payless Office Products (Payless) non-core catalog items was not monitored to see that the county was receiving the appropriate discount. (Internal Audit did obtain reporting from Payless showing the gross profit margin for products purchased in 2013; the margins were within the contractual percentage to yield the proper discount.)
- There was no verification to see that the sales totals used by Payless to calculate the volume rebate amounts were correct.
- The Payless performance bond was expired and the certificate of insurance did not include professional liability insurance as required per the contract. (Payless later updated the performance bond and forwarded evidence of it to the County.)
- For two of the three periods tested, Midwest Independent Physicians (MIP) billed the maximum number of physician hours per the contract. About half of the hours billed was for administrative work not conducted at the clinic. The contract allows billing for administrative work outside of the clinic, but MIP did not provide documentation of the administrative work that was actually performed. (MIP cut their administrative hours approximately one half in subsequent billings – a reduction of over \$1,000 for each biweekly billing.)
- Lifecare Family Medicine of Bellevue did not provide a certificate of insurance showing the County as an additional insured as required per the contract. (A certificate of insurance was later obtained showing the County named as an additional insured as required by the contract.)

- Aramark Correctional Services did not initially provide a certificate of insurance as required per the contract. (A certificate of insurance was later obtained showing the County as an additional insured with the coverage as required per the contract.)

Effect: Results of ineffective monitoring included the following:

- Waste Management overbilled the County \$21, 867 (from May 2013 – October 2013) for the Final Phase of the Omaha Lead Clean-up Project. (Upon notification, Waste Management issued a correction and a credit in subsequent invoices.)
- The public did not have a chance to attend and provide input in regard to Waste Management’s contract performance. (An annual evaluation has been scheduled for January 7, 2014.)
- If Petroleum Traders gasoline deliveries continued beyond the contractual quantity, the County could suffer a financial loss if current prices were less than the contractual price and Petroleum Traders continued to bill at the contractual price.
- Without obtaining the appropriate gross profit documentation from Payless, the County could not be sure that it obtained the appropriate product discounts.
- If erroneous sales information was used to calculate the Payless volume discount, it may not be detected by management and result in an incorrect rebate. (Audit testing revealed that the sales volume used to calculate the rebate was correct.)
- Without appropriate documentation, the administrative work that MIP billed for could not be evaluated to determine if the number of hours was reasonable.
- Without the appropriate certificates of insurance and performance bonds, the County could not be sure that there was adequate insurance and bond coverage to protect the County.

Cause: Management relied on the skills of department personnel to monitor contracts, but did not provide appropriate guidance or training to help ensure personnel understood all aspects of how to effectively monitor contract compliance.

Recommendation: Formally document the policies and procedures needed to effectively monitor contract compliance including assigning responsibilities to appropriate personnel. Train personnel in the proper use of the policies. The policies should include instructions that will answer the following questions:

- Who has overall responsibility for ensuring that contractual obligations are met?
- Who will monitor operational performance?
- What are the key deliverables that need to be monitored?
- How will the deliverables be monitored and how often will it need to be done?
- If appropriate, has an appropriate plan been prepared (e.g., milestones, timelines, dependencies etc.)?
- Are there unique accounting, purchasing, or other aspects that need to be communicated to other personnel within the County?
- Who will approve billings/payments?
- Who will verify the accuracy of the billings/payments and how will it be accomplished?
- Is there an appropriate problem/dispute resolution plan in place including how to identify contract noncompliance?

- What documentation needs to be obtained and maintained within the department or forwarded to other departments or entities to ensure contract compliance and billing/payment accuracy, and who will obtain the documentation?
- How will timely procurement of key contractual obligations be ensured (e.g., continued performance bond and insurance coverage)?

Additionally, management should take specific steps to address specific findings which include the following:

- Use the existing Faster system or another process to track fuel deliveries per contractual obligations.
- Establish a policy to obtain and analyze Payless gross margin and verify the vendor purchases used to calculate the volume discount rebate.

Management Response: Purchasing agrees with the recommendations regarding the need to better define and communicate the necessary policies and guidelines needed to effectively monitor contract compliance including vendor billings. To that end, Purchasing has formed a committee including Buyers and the Contract Administrator to create a formal process for Bids/RFPs, to include contract monitoring and updating of Insurance and Performance Bonds. The procedures will also address assigning responsibilities to appropriate personnel and training personnel in the proper use of the policies. Purchasing Agent is also reviewing the process to track fuel deliveries under current and future vendor contracts with County Garage and City Fleet Management staff. Finally, Purchasing staff is working closely with Payless management to schedule regular reporting to the County for the purpose of validating Payless gross margin as it relates to our volume discount rebate.

Payless Contract Opportunities

Criteria: Management should take advantage of all reasonable, savings opportunities.

Condition: The Payless contract provides the opportunity to take a 1% discount for paying billings within 10 days of billing date. The County does not take advantage of this discount. Additionally, there are substantial savings that can be obtained by selecting Private Brand Products on individual purchases when they are offered. The Payless representative stated that the County uses this option infrequently.

Effect: Based upon the total purchases from calendar year 2012, the County has lost over \$4,000 by not using the 1% prompt payment discount. Potentially, much larger savings were lost by infrequent use of the Private Brand Products option.

Cause: The current process in place is not designed to consistently pay bills within 10 days. Current policies and procedures for ordering office supplies do not require or enforce the purchase of Private Brand Products when available.

Recommendation: Use the monthly billing option as provided for in the contract to receive the 1% prompt payment discount. Train the individual department personnel regarding changes that may be needed to ensure prompt payment. Use the Payless website option that will force users

to select Private Brand Products for those items that are judged equivalents and can provide significant savings.

Management Response: Purchasing understands that the current billing to individual departments is not conducive to taking advantage of the 1% discount as it can only be earned by paying early for the entire County Account, not individual departments. Purchasing is working with Payless on a strategy to feature Private Brand Products through the existing on-line catalog where reasonable to increase savings opportunities. We will consider the use of substitute items as a way of driving increased use of these Private Brand Products to lower departmental costs.

Audit Standards

Internal Audit conducted this audit in accordance with generally accepted government auditing standards. Those standards require that the audit is planned and performed to obtain sufficient, appropriate evidence to provide a reasonable basis for the findings and conclusions based on the audit objectives. Internal Audit believes that the evidence obtained provides a reasonable basis for its findings and conclusions based on the audit objectives. This report was reviewed with Director of Corrections, Mark Foxall, Environmental Services Director, Kent Holm, Director of General Assistance, Deb Redding, Interim Director of Community Mental Health Center, Sherry Glasnapp, and Purchasing Agent, Eric Carlson.

Internal Audit appreciates the excellent cooperation provided by the various departmental directors and staff. If you have any questions or wish to discuss the information presented in this report, please feel free to contact me at (402) 444-4327.

Sincerely,

Mike Dwornicki
Internal Audit Director

cc: Paul Tomoser
Trent Demulling
Joni Davis
Donald Stephens
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